PREFILED WRITTEN TESTIMONY
GENE E. BAUER, PH.D., MANAGING DIRECTOR
HAY GROUP, INC.

Hay Group, Inc. is a privately-held global consulting firm of over 2,000 consultants, including academicians, accountants, actuaries, attorneys, economists, executives, human resource specialists, psychologists and researchers, helping organizations design and implement strategies to organize, manage, motivate and reward people. Hay Group, Inc. has 72 offices in 35 countries around the world and works with all types of organizations, including large and complex companies, as well as substantially smaller local businesses across industry sectors, such as healthcare, retail, manufacturing and financial services.

Hay Group, Inc. works with boards of directors, compensation committees and senior executives to set compensation packages that motivate and reward those who run businesses in terms that are clearly justifiable to shareholders or stakeholders. The Executive Compensation Practice is dedicated to three critical needs of executive compensation: (1) supporting business strategies with effective compensation and benefits programs; (2) providing market data, practices and trends and interpreting the implications of market practice given a client's particular situation; and (3) providing complete knowledge of accounting, tax, securities and other regulatory areas. The executive compensation consultants work extensively with management, boards of directors and compensation committees on issues such as: (1) sharing competitive data and practices, along with trends and best practices; (2) discussing and supporting compensation decisions for individuals, the executive group or employees generally; (3) presenting and discussing new compensation and benefits programs in which executives participate and the programs' support of the business strategy; and (4) synthesizing technical implications of executive compensation.

In November, 1999, the Board of Directors of CareFirst, Inc. engaged Hay Group, Inc. to assist management and the Executive Compensation Committee of the Board of Directors in reviewing and evaluating the company's compensation arrangements and benefit programs. Based on a thorough review of the CareFirst compensation arrangements and comparable compensation arrangements for similar corporations, Hay Group has concluded that the compensation arrangements in place at CareFirst relating to the acquisition of the company are justifiable, appropriate and commercially reasonable. Ultimately, these compensation arrangements inure to the public benefit because they serve to maximize the value of CareFirst's public or charitable assets for the direct benefit of the owners of these assets – the State of Maryland, the State of Delaware and the District of Columbia – by helping to retain critical executives and providing incentives to top management to secure the full market value in a transaction.

1. Incentive and Retention Plans Relating to the Acquisition of CareFirst

As part of its engagement, Hay Group was asked by the Executive Compensation Committee of the CareFirst Board of Directors to analyze recent retention bonuses provided by other health services and health insurance organizations going through a merger and to make recommendations to the Committee regarding the appropriate level of merger incentive and retention bonuses for CareFirst officers and senior managers. On April 20, 2001, Hay Group presented its findings and recommendations to the Executive Compensation Committee, which approved the recommendations. On April 26, 2001 and, again on July 26, 2001, the findings and recommendations of the Hay Group were reported to the CareFirst Board of Directors.[1]

Acting upon these recommendations, on July 26, 2001, the CareFirst Board of Directors approved a merger incentive plan for the chief executive officer and the executive vice presidents and a retention bonus plan for senior vice presidents, vice presidents and senior managers. No individual participates in both plans, and the CareFirst Board of Directors does not participate in either plan.[2]

Merger Incentive Plan[3]

The Merger Incentive Plan provides that, following the sale or disposition of the company, a merger incentive, calculated as a percentage of the merger consideration, will be paid to the following participants:[4]

William L. Jews	President and Chief Executive Officer
David D. Wolf	Executive Vice President, Managed Care and Strategic Planning
Leon Kaplan	Executive Vice President, Operations
Gregory A. Devou	Executive Vice President and Chief Marketing Officer
G. Mark Chaney	Executive Vice President, Chief Financial Officer and Treasurer
John A. Picciotto	Executive Vice President, General Counsel & Corporate Secretary
Sharon J. Vecchioni	Executive Vice President, Chief of Staff

The purpose of the Merger Incentive Plan is to align the interests of CareFirst's executive management team with the interests of the stakeholders to ensure that the executive management

1 Hay Group, Inc. memorialized its confidential report on merger bonuses in a letter to the Executive Compensation Committee, dated July 30, 2001, which is attached as Exhibit 1 to this testimony.

2 The Board of Directors amended the plans on November 20, 2001, in conjunction with the approval of the WellPoint transaction. The plan documents were executed on December 2, 2001.

3 A copy of the Merger Incentive Plan, together with the letters of participation for each participant in the Merger Incentive Plan, is attached as Exhibit 2 to this testimony.

4 The participants in the Merger Incentive Plan are considered the CareFirst "executive management team." The executive management team has management responsibility for four companies: CareFirst, Inc., CareFirst of Maryland, Inc., Group Hospitalization and Medical Services, Inc., and Blue Cross Blue Shield of Delaware, Inc.

team will aggressively pursue a transaction that may be in the best interests of the stakeholders. In any sale transaction, the board of directors and the stakeholders must depend on the executive management team to negotiate and present the best possible transaction. However, such a transaction may not be in management's best interests since, oftentimes in these transactions, members of the executive management team will lose their jobs or have reduced titles and positions after the transaction. As a result, management may, in effect, be negotiating a transaction that will not be in their best interests, from a personal standpoint. Thus, any such transaction puts management at risk. Moreover, there is always the possibility that a potential buyer will attempt to negotiate the terms of future employment with members of the executive management team before the sale terms are finalized. The possibility of such negotiation may create a potential for a conflict of interest.

While "change-of-control" severance arrangements such as those in place at CareFirst provide some benefits to members of the executive management team, those benefits are paid only if the executive's employment is terminated. Those arrangements do not align the interests of the executive management team with the interests of stakeholders to ensure that the executive management team will aggressively pursue the best transaction for the stakeholders. The Merger Incentive Plan assures that the executive management team has no disincentive to investigate and to consummate the best transaction for the stakeholders from a financial standpoint. The Merger Incentive Plan also gives the executive management team an additional incentive during a lengthy review period to conduct company operations in a manner to keep the organization successful and attractive both to its proposed acquirer (which might otherwise seek to abandon the transaction) and to potential alternative partners. Such incentives are commonplace, commercially reasonable and appropriate in today's market and reflect the level of skill, effort, dedication and time required to consummate a successful merger. Those incentives are especially important in connection with the CareFirst acquisition because the complex nature of the CareFirst acquisition, involving as it does multiple regulatory jurisdictions and approvals, creates a very lengthy period of uncertainty.

Based on our experience as management consultants, we are convinced that the best way to maximize the merger consideration in a transaction of this sort, which in this case inures directly to the State of Maryland, the State of Delaware and the District of Columbia as the ultimate stakeholders, is to provide a financial incentive to the executive management team. Tying this financial incentive directly to the amount of merger consideration is the best encouragement available to the executive management team to maximize the merger consideration for the benefit of the stakeholders.

Hay Group was asked by the Executive Compensation Committee to recommend the appropriate level of merger incentive to members of the executive management team under the Merger Incentive Plan. To do so, Hay Group reviewed 13 merger transactions for 13 health services or health insurance organizations since January 1, 1996, including the recent acquisition of Cerulean Companies, Inc. (the Georgia Blue Cross Blue Shield plan) by WellPoint. The median equity-based compensation for the chief executive officer of the acquired entity in these transactions is 0.88% of the merger consideration. The median equity-based compensation for the executive management team (including the chief executive officer) of the acquired entity in these transactions is 2.38% of the merger consideration. The equity-based compensation for the chief executive officer of Cerulean was 0.94% of the merger consideration. The equity-based compensation for the executive management team (including the chief executive officer) of Cerulean was 2.55% of the merger consideration.[5]

Under the Merger Incentive Plan, the CareFirst Board of Directors granted Mr. Jews a merger incentive equal to 0.70% of the merger consideration and granted an aggregate merger incentive to the executive management team (including Mr. Jews) equal to 1.90% of the merger consideration. The merger incentive payable to the CareFirst executive management team under the Merger Incentive Plan (expressed as a percentage of merger consideration) is 20% less than the median equity-based compensation for the executive management team of the acquired entity in the 13 comparable merger transactions we reviewed and 25% less than the equity-based compensation for the executive management team of Cerulean. We conclude that the level of merger incentive under the Merger Incentive Plan is both reasonable and appropriate when compared to executive compensation in comparable circumstances.[6]

Assuming a merger consideration of $1,300,000,000, each participant will receive the following merger incentive based on the percentage granted each participant under the terms of the Merger Incentive Plan:[7]

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5 "Equity-based compensation" is the appreciation in value of stock options and stock (often restricted) in the acquired company, as well as phantom stock and similar awards, held by an executive of the acquired company from a date prior to the commencement of merger negotiations to the date on which the merger is consummated.

6 Further to determine the appropriate merger incentive to be paid to Mr. Jews, CareFirst, through its attorneys, Piper Marbury Rudnick Wolfe, sought the opinion of Frederic W. Cook & Co., Inc., also a nationally-recognized executive compensation firm. Frederic W. Cook & Co., Inc. concluded that a merger incentive to Mr. Jews equal to 0.75% of the merger consideration is commercially reasonable and appropriate. A copy of the Frederic W. Cook & Co., Inc. memorandum, dated April 12, 2001, together with a brief description of the firm, is attached as Exhibit 3 to this testimony.

7 Under the terms of the employment agreements each of these executives has with CareFirst, the executives are also entitled to reimbursement for any federal excise tax imposed under Section 4999(a) of the Internal Revenue Code (together with reimbursement for any taxes attributable to the reimbursement for the federal excise tax) if the merger incentive is deemed an "excess parachute payment."

William L. Jews	$ 9,100,000	0.70000%
David D. Wolf	$ 3,600,000	0.27692%
John A. Picciotto	$ 2,800,000	0.21538%
Leon Kaplan	$ 2,300,000	0.17692%
Gregory A. Devou	$ 2,300,000	0.17692%
G. Mark Chaney	$ 2,300,000	0.17692%
Sharon J. Vecchioni	$ 2,300,000	0.17692%
	$24,700,000	1.90000%

Under the terms of the Merger Incentive Plan, as amended by the CareFirst Board of Directors in connection with the WellPoint transaction, the foregoing merger incentive will be paid in restricted shares of WellPoint common stock issued within five business days after closing and vesting in equal annual installments as of the first, second and third anniversaries of the closing date of the transaction if the participant remains employed by the company through the vesting dates. The restricted shares become fully vested if (i) the participant remains employed by WellPoint for three years after the closing date of the transaction or (ii) the participant's employment is terminated within this three-year period either by the company without "cause" or by the participant for "good reason." [8]

Mr. Jews will receive a cash payment if he terminates his employment other than for "good reason" on or after the closing date of the transaction, but before the third anniversary of the closing date of the transaction. The amount of the cash payment will depend on whether restricted shares of WellPoint common stock have been issued to Mr. Jews and to what extent they are vested. If Mr. Jews terminates his employment other than for "good reason" on or after the closing date of the transaction, but before the third anniversary of the closing date of the transaction, the value of the restricted shares of WellPoint common stock issued to Mr. Jews that

[8] "Good reason" includes, among other things, (i) a material reduction in the participant's responsibilities, duties, or authority; (ii) a transfer to a location that results in a commuting distance that is more than 50 miles greater than the commuting distance as of the effective date of the plan; or (iii) a failure to provide a compensation arrangement that is comparable to similarly situated employees.

are vested as of the date of termination (valued as of the date of issuance), together with the cash payment, will equal the full amount of the merger incentive due Mr. Jews under the Merger Incentive Plan.[9]

Retention Bonus Plan[10]

The Retention Bonus Plan provides that, following the sale or disposition of the company or a determination by the CareFirst Board of Directors to abandon pursuit of a sale or disposition, a retention bonus, calculated as a percentage of base salary, will be paid to selected senior vice presidents, vice presidents and senior managers.

The purpose of the Retention Bonus Plan is to provide financial incentives to key employees of CareFirst (other than the executive management team) to secure their commitment and dedication, to enlist their support in locating a strategic partner or buyer and to ensure that they conduct the affairs of the company in such manner as to maintain the highest possible value of the public or charitable assets for the benefit of the State of Maryland, the State of Delaware and the District of Columbia. The Retention Bonus Plan also seeks to retain these key employees in the event the transaction does not close so that the company and its owners will continue to have a strong management system in place to maintain operations following an unconsummated transaction. These key employees are highly vulnerable to recruitment by other organizations (including competitors) during this period of great uncertainty and the Retention Bonus Plan gives them a direct incentive to remain at CareFirst until the transaction either closes

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[9] Any other participant in the Merger Incentive Plan who terminates employment other than for "good reason" receives, as a merger incentive, only the restricted shares of WellPoint common stock that have vested as of the date of termination.

[10] A copy of the Retention Bonus Plan is attached as Exhibit 4 to this testimony. As of the date of this testimony, there are no letters of participation for the Retention Bonus Plan.

or is abandoned. Such plans are common among both closely-held and publicly-held corporations to maintain stakeholder value during the sale and disposition process.

As adopted by the CareFirst Board of Directors, the aggregate projected amount payable to participants under the Retention Bonus Plan after the WellPoint transaction closes or pursuit of the transaction is abandoned by the Board of Directors is $8,469,000, distributed as follows:[11]

Senior Vice Presidents (8)	1.5 x Base Salary	$2,895,000
Vice Presidents (23)	1.0 x Base Salary	$3,877,000
Directors (36)[12]	0.5 x Base Salary	$1,697,000

To advise the CareFirst Board of Directors on the appropriate level of retention bonus, Hay Group relied, among other things, upon data secured in 2000 through Executive Compensation Advisory Services, regarding merger and acquisition retention awards, which included information on retention awards paid by organizations of similar size and complexity to CareFirst that had completed mergers or similar transactions. Hay Group recommended a retention award for senior vice presidents and vice presidents equal to one year's base salary and a retention award for other selected individuals equal to a half year's base salary. Although the Board adopted a Retention Bonus Plan that pays more to senior vice presidents than we initially recommended, Hay Group concludes that the retention bonuses payable to CareFirst senior vice presidents, vice presidents and senior managers under the Retention Bonus Plan are reasonable and appropriate in light of the difficulty of and uncertainty attendant to this transaction.

In order for the participant to receive the retention bonus, either (i) the Board of Directors abandons pursuit of a sale or disposition of the company or (ii) the transaction closes, (A) the

11 These projected amounts are based on estimates made by CareFirst in April, 2001. No final decision has yet been made by CareFirst as to who will participate in the Retention Bonus Plan.

12 Although not officers of the company, directors are senior management personnel. CareFirst currently has approximately 100 directors. It is estimated by management that approximately 36 will be selected to participate in the Retention Bonus Plan.

participant must be employed continuously through the day immediately preceding the closing date or (B) the participant's employment must be terminated without "cause" by the company or, if the participant holds the title of senior vice president or higher, for "good reason" by the participant during the 12 months immediately preceding the closing date.[13] The retention bonus is payable to participants no later than the fifth business day following the closing date or the date fixed by the CareFirst Board of Directors if it determines to abandon the pursuit of the transaction.

Aggregating the projected payments under the Merger Incentive Plan and the Retention Bonus Plan, one may expect that these payments will equal approximately $33,169,000 or 2.55% of the merger consideration. By contrast Cerulean awarded $30,027,030 (or 4.29% of the merger consideration) to its key executives alone and another $17,862,970 to other employees. In total, Cerulean paid $47,890,000 (or 6.84% of the merger consideration) in merger-related incentives. Given that the merger consideration in the WellPoint-Cerulean transaction was only $700,000,000, the incentives payable in this transaction under the Merger Incentive Plan and the Retention Bonus Plan are reasonable.

2. "Change-of-Control" Termination Payments to Certain CareFirst Executives

Each member of the executive management team and Michael J. Felber, Senior Vice President, Sales, have a written employment agreement with CareFirst. In addition, Thomas C. Rekart, Senior Vice President & Chief Information Officer, and Booker T. Carter, Senior Vice

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13 "Good reason" includes, among other things, (i) a material reduction in the participant's responsibilities, duties, or authority; (ii) a transfer to a location that results in a commuting distance that is more than 50 miles greater than the commuting distance as of the effective date of the plan; or (iii) a failure to provide a compensation arrangement that is comparable to similarly situated employees of the company.

President, Claims & Service, have a written "change-of-control" agreement.[14] These agreements were in place prior to the initiation of merger negotiations between CareFirst and WellPoint.

Each employment agreement provides for termination benefits if the executive's employment is terminated without "cause" by the company or for "good reason" by the executive within 12 months before or 24 months after a "change of control."[15] Each "change-of-control" agreement provides for termination benefits if the executive's employment is terminated without "cause" by the company or for "good reason" by the executive within 90 days before or 12 months after a "change of control."[16] The acquisition of CareFirst by WellPoint, as contemplated in the Agreement and Plan of Merger dated November 20, 2001, constitutes a "change of control" under the agreements.

Under the employment agreements, if the executive's employment is terminated by the company without "cause" or by the executive for "good reason" within 12 months before or 24 months after a "change of control," the executive is entitled to the following termination benefits: (i) a severance payment that is a multiple of the executive's base salary (a portion of

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[14] A copy of the employment agreements and the "change-of-control" agreements is attached as Exhibit 5 to this testimony.

[15] Under the terms of the employment agreements, termination benefits are payable if the executive's employment is terminated because of death or disability, for "cause" or other than for "good reason," without "cause" or for "good reason" (not in connection with a "change of control"), or without "cause" or for "good reason" (in connection with a "change of control"). The benefits payable to the executive differ based on the reason for the termination.

[16] "Good reason" includes, among other things, (i) a material reduction in the executive's responsibilities, duties, authority, or title; (ii) a transfer to a location that results in a commuting distance that is more than 50 miles greater than the commuting distance as of the date of the employment agreement; or (iii) a reduction in salary or a material diminution in benefits. "Good reason" also exists if, after the "change of control," the executive does not continue to hold the executive position with the most senior resulting entity that the executive holds with CareFirst under the employment agreement. In the employment agreements (but not in the "change-of-control" agreements) the acceptance of a new position with the most senior resulting entity is not deemed a waiver of the executive's right to terminate employment and receive the severance payment if the termination occurs within 24 months after the "change of control." We have been advised by CareFirst that none of the executives entitled to termination payments in connection with a "change of control" will hold the executive position with WellPoint that the executive holds with CareFirst.

which is paid in consideration of a covenant by the executive not to compete with the company for a specified period) and a multiple of the executive's target award under the company's annual incentive plan; (ii) except if the termination occurs during the first three months of the year, a payment under the annual incentive plan for the year in which the termination occurs; (iii) a payment for the amount due under the Long-Term Performance Incentive Plan;[17] (iv) personal and health benefits; and (v) an immediate benefit under the CareFirst, Inc. Executive Retirement Plan without reduction based on the executive's age.[18] Termination benefits provided under the "change-of-control" agreements are comprised of the same elements, except that the executive does not receive a payment under the annual incentive plan for the year in which the termination occurs or personal benefits. In addition, under the "change-of-control" agreements the executive receives a benefit under the CareFirst, Inc. Executive Retirement Plan that is consistent with the Plan rather than an immediate benefit without reduction based on the executive's age.

The projected amount each executive would receive as a termination payment if the executive's employment were terminated by the company without "cause" or by the executive for "good reason" within the specified period before or after the closing date of the WellPoint transaction has been determined by CareFirst to be as follows:[19]

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17 A copy of the Long-Term Performance Incentive Plan is attached as Exhibit 6 to this testimony.

18 A copy of the CareFirst, Inc. Executive Retirement Plan is attached as Exhibit 7 to this testimony.

19 The stated amounts assume that the executive's employment terminates as of April 1, 2003, which was the projected closing date of the transaction when these calculations were undertaken in April, 2001. Under the terms of the agreements each of these executives has with CareFirst (except Michael J. Felber), the executives are also entitled to reimbursement for any federal excise tax imposed under Section 4999(a) of the Internal Revenue Code (together with reimbursement for any taxes attributable to the reimbursement for the federal excise tax) if the termination payment is deemed an "excess parachute payment." Under Mr. Felber's employment agreement, if the termination payment is deemed an "excess parachute payment," the amount of the termination payment is reduced in the amount necessary to avoid the federal excise tax.

William L. Jews	$ 18,600,000
David D. Wolf	$ 6,140,000
Leon Kaplan	$ 4,730,000
Gregory A. Devou	$ 4,900,000
G. Mark Chaney	$ 4,500,000
John A. Picciotto	$ 2,090,000
Sharon J. Vecchioni	$ 2,880,000
Michael J. Felber	$ 1,680,000
Thomas C. Rekart	$ 1,260,000
Booker T. Carter	$ 1,090,000

It is important to emphasize that these projected amounts are only payable if the executive's employment with the company terminates. If the executive remains employed with the company after the WellPoint transaction, the executive receives no "change-of-control" payment, except for the payment due under the terms of the Long-Term Performance Incentive Plan that has been earned and becomes vested as a result of the change of control.[20]

Hay Group was asked by the Executive Compensation Committee if the projected amounts payable at termination in connection with a "change of control" are commercially reasonable and appropriate under the circumstances. It is our opinion that these amounts are commercially reasonable and appropriate under the circumstances. The termination payments resulting from a "change of control" are based upon each executive's actual compensation. Hay Group has reviewed the compensation levels for these executives and has found them to be within appropriate norms for similarly-sized corporations. Further, the components of the "change-of-control" provisions in the employment agreements of CareFirst executives are

[20] It is also important to note that, under the terms of the employment agreements, the major portion of these projected amounts would be payable to the executives upon termination without "cause" or for "good reason" even if there were no "change of control." As demonstrated by the charts attached as Exhibit 8 to this testimony, only a minor portion of the termination payment is directly attributable to the "change of control."

comparable to the components of "change-of-control" provisions in executive employment agreements at similarly-sized corporations.[21]

In this case, the "change-of-control" provisions are clearly in the best interests of the State of Maryland, the State of Delaware and the District of Columbia (the ultimate CareFirst stakeholders) as well as CareFirst subscribers. They help ensure that critical contributors and leaders are kept in place and productive during a time of great uncertainty and insecurity. In addition, they free senior executives from any conflict the executives may otherwise feel as to whether a proposed transaction is in their own best interest.[22] These contractual provisions were put in place long before CareFirst's negotiations with WellPoint began. They were designed to assure stability during a time in which there was no certainty as to the identity of any strategic partner. They will remain in place throughout a period of further uncertainty caused by a lengthy and complex multi-jurisdictional regulatory review process.

Retaining stable leadership free of conflict in a time of great uncertainty helps keep strategy and performance on track. Retention of senior executives is critical to CareFirst's success even if the WellPoint transaction fails to close. More importantly, however, retention of senior executives maximizes CareFirst's value to buyers and investors, which in turn maximizes the value of CareFirst's public or charitable assets to the State of Maryland, the State of Delaware and the District of Columbia.[23]

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[21] In at least 11 of the 13 merger transactions examined by Hay Group in recommending a merger incentive, some members of the executive management team were entitled to receive "change-of-control" termination payments under existing arrangements in addition to the equity-based compensation. As to the remaining two merger transactions, information was not available on this point.

[22] For example, if a senior executive believes that he will lose his job if the transaction is completed, he may not work to accomplish it absent the protection afforded by the "change-of-control" provision even though the transaction may be in the best interest of the shareholders/owners.

[23] A copy of Hay Group, Inc.'s confidential report to the Executive Compensation Committee, dated February 11, 2002, relating to "change-of-control" termination payments, is attached as Exhibit 9 to this testimony.

Respectfully submitted,

Gene E. Bauer, Ph.D., Managing Director
Hay Group, Inc.

March 6, 2002